



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

201249018

DEC 28 2011

UIL: 419.00-00; 419.05-00; 419A.00-00

T.E.P. RA: T2

LEGEND

Company =

Note =

Trust =

Amount A =

Amount B =

Amount C =

Entity 1 =

Date A =

Loan Terms A=

Loan Terms B =

Loan Terms C =

Loan Terms D =

Loan Terms E =

Dear :

This is in response to a request submitted on your behalf by your authorized representatives dated as supplemented by additional correspondence dated , in which you requested a private letter ruling to supplement (the Prior Ruling), which was previously issued to you.

As described in more detail below, the Prior Ruling addressed, among other things, the tax treatment of the contribution of Note to Trust. Your ruling request concerns the tax treatment of prepayment of Note, and the tax treatment of a transfer of Note by Trust to a third party.

FACTS

The background facts are set forth in the Prior Ruling.

The following facts and representations have been submitted under penalty of perjury in support of the ruling requested:

Pursuant to a settlement agreement, Company became obligated to contribute Note to Trust to provide for Trust's payments of employees' post-retirement medical benefits. Or Date A, Company contributed Note to Trust with a principal amount of Amount A, and an implied Amount B interest rate payable in Amount C Loan Terms A installments Loan Terms B. The interest rate payable on Note was greater than the long-term applicable Federal rate in effect for Date A. The Note indenture provides that Note is Loan Terms C and prepayable at any time. Company has a right of first offer (ROFO) in the event that Trust wishes to dispose of all or a portion of Note to a third party for cash. The holder of Note may demand that Company Loan Terms D. The Loan Terms E.

The Prior Ruling addresses, among other things, the tax treatment of Company's contribution of Note to Trust. The Prior Ruling concluded that "each annual installment on Note paid to Trust is a contribution to Trust," and "[e]ach such contribution is deductible by Company, subject to any capitalization requirement generally applicable to such contributions under section 263A of the Code or otherwise, pursuant to sections 419 and 419A of the Code for the taxable year in which the installment payment is made to Trust." The Prior Ruling further states that each such contribution was only deductible "to the extent that, as of the date of the contribution, the amount of the contribution does not exceed the unfunded present value of benefits to be provided through Trust". The Prior Ruling does not address the consequences of a prepayment or transfer of Note to a third party. You represent that events subsequent to the Prior Ruling have increased the likelihood that Note will be transferred or prepaid. You have asked us to assume, and we are so assuming, that any transfer would be solely for cash.

RULINGS REQUESTED

- 1) Upon prepayment of Note (or portions thereof) in cash by Company pursuant to the Note indenture and/or repurchase of Note by Company pursuant to the right of first offer, such prepayment is deductible by Company in the taxable year in which it is made, subject to any capitalization requirement otherwise applicable to Note, and provided that the amount of the prepayment does not exceed the unfunded present value of benefits to be provided through the Trust as of the date of prepayment.
- 2) The cash proceeds received by Trust from a transfer constitute a contribution by Company to Trust, and such contribution (in the amount of such transfer proceeds) is deductible by Company in the taxable year in which the transfer is made, subject to any capitalization requirement otherwise applicable to Note, and provided that the amount of cash proceeds does not exceed the unfunded present value of benefits to be provided through Trust as of the date of transfer.
- 3) Upon the sale of Note by Trust (other than pursuant to the right of first offer), Company is considered to have issued a debt instrument to the transferee of Note with terms identical to those remaining on Note as of the transfer date and with an issue price equal to the amount of the transfer proceeds.

LAW

Section 162(a) of the Internal Revenue Code provides for a deduction for all ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. Section 1.162-10T, Q&A-2 of the Income Tax Regulations provides that section 419 governs the deduction of contributions paid or accrued by an employer with respect to a "welfare benefit fund" within the meaning of section 419(e).

Section 419(a) provides that contributions paid or accrued by an employer to a welfare benefit fund are not deductible under Chapter 1 , but if they would otherwise be deductible shall (subject to the limitation in section 419(b)) be deductible under section 419 for the taxable year when paid.

Section 1.419-1T, Q&A-10(a) states in part that contributions paid or accrued with respect to a welfare benefit fund are deductible only to the extent that the contributions satisfy the requirements of section 162 or 212.¹

Section 1.419-1T, Q&A-10(d) provides that in determining the extent to which contributions paid or accrued with respect to a welfare benefit fund are deductible under section 419 , the rules of sections 263, 446(b), and 461(a) will be treated as having been satisfied to the extent the contributions satisfy the otherwise applicable rules of section 419 . Thus, for example, contributions to a welfare benefit fund will not fail to be deductible under section 419 merely because they create an asset with a useful life extending substantially beyond the close of the taxable year if such contributions satisfy the otherwise applicable requirements of section 419.

ANALYSIS

Ruling Request #1

The Prior Ruling held that each annual installment payment on Note was deductible by Company as a contribution to Trust, under sections 419 and 419A, in the taxable year in which made (subject to the limitations stated above). The same analysis applies to a prepayment of Note as would apply to each annual installment. Making payments in advance, pursuant to a prepayment provision in the Note indenture or a right of first offer, does not adversely affect the deductibility of the payment.

Accordingly, upon prepayment of Note (or portions thereof) in cash by Company pursuant to the Note indenture, and/or the repurchase of Note by Company pursuant to the right of first offer, such prepayment is deductible by Company in the taxable year in which it is made, subject to any capitalization requirement otherwise applicable to Note, and only to the extent that the amount of the prepayment does not exceed the unfunded present value of benefits to be provided through Trust as of the date of prepayment.

Ruling Request #2

Section 419(a) provides that “contributions paid or accrued by an *employer*” (emphasis added) are deductible for the taxable year when paid, subject to the other limitations of section 419. If Trust transfers Note to a third party, the third party will pay Trust for Note, and thereafter Company will pay annual installments to the third party. For purposes of section 419, “payment” by Company is considered to occur when Trust receives the payment from the third party.

¹ The Regulations refer to deductibility under sections 162 and 212 (rather than “otherwise” deductibility) because they were published before technical corrections of section 419(a) were enacted.

This approach is consistent with the policy of Don E. Williams v. Comm'r, 429 U.S. 569 (1977), which interpreted the analogous "payment" requirement in section 404. The Supreme Court explained that the policy behind the payment requirement is to "insure the integrity of the employees' plan and insure the full advantage of any contribution which entitles the employer to a tax benefit." Id. at 579. Here, when Note is transferred to a third party, and the third party pays proceeds to Trust, Trust will get the full advantage of the contribution that entitles Company to a tax benefit.

Accordingly, any cash proceeds received by Trust from a transfer of Note to a third party constitute a contribution by Company to Trust, and such contribution (in the amount of such transfer proceeds) is deductible by Company in the taxable year in which the transfer is made, subject to any capitalization requirement otherwise applicable on Note, and only to the extent that the amount of the cash proceeds does not exceed the unfunded present value of benefits to be provided through Trust as of the date of transfer.

Ruling Request #3

Because the contribution of Note to Trust does not by itself represent a paying out or reduction of Company's assets under Williams, the contribution of Note by Company to Trust is not a transfer of property. However, this special treatment of Note is no longer applicable when Note is transferred to a third party because the policy of Williams would no longer apply to a transferee that is not a welfare benefit fund or similar entity. Under the second ruling above, Company, in effect, is treated as receiving the cash proceeds from the third party in exchange for a new note and then contributing the cash proceeds to Trust as a prepayment on Note. Therefore, upon a transfer of Note to a third party, Company is treated for federal income tax purposes as incurring new indebtedness in respect of the third party transferee (that is, as if Company issued a new Note to the transferee third party with an issue price equal to the transfer proceeds and with terms identical to those remaining on Note as of the transfer date).

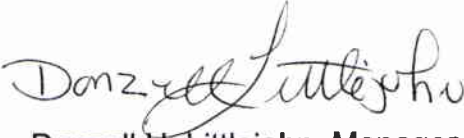
Except as specifically ruled above, no opinion is expressed as to the federal tax consequences of the transaction described above under any other provision of the Internal Revenue Code or as to the consequences under Title I of ERISA. Specifically, no opinion is expressed regarding whether part or all of the contributions to Trust must be capitalized under section 263A.

Pursuant to a power of attorney on file with this office, a copy of this letter ruling is being sent to your authorized representatives.

This letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Please contact _____ at _____ with any questions about this letter.

Sincerely yours,

A handwritten signature in cursive script, reading "Donzell H. Littlejohn".

Donzell H. Littlejohn, Manager
Employee Plans Technical Group 2

Enclosures:

Deleted copy of letter ruling
Notice of Intention to Disclose